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C O N F I D E N T I A L SECTION 01 OF 03 KUWAIT 000786

SIPDIS

STATE ALSO PASS TO DEPT OF ENERGY
PENTAGON FOR DESC

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SUBJECT: (SBU) KUWAIT AND IRAQ BEGIN ADDRESSING BILATERAL
ENERGY CONCERNS

REF: KUWAIT 05756

Classified By: DCM FRANK C URBANCIC; REASON 1.4 (B)

11. (SBU) Summary. Energy Ministry Undersecretary Al-Own told USG officials that Kuwait and Iraq have begun direct discussion of bilateral energy issues through the creation of a technical committee, but he remains concerned that Iraq is lacking well-organized plans for the sector. (See septel on Ambassador's March 8 meeting with Kuwaiti Energy and Iraqi Electricity Ministers in Kuwait City.) Of primary immediate concern for the bilateral technical committee is planning the supply of fuels from Kuwait to Iraq to begin 1 April and most likely to continue after the dissolution of the CPA in Iraq on 30 June. Al-Own confirmed that any firm could bid on humanitarian fuel contracts tendered by the USG and its agents. Al-Own said the technical committee is considering the longer term exportation of Iraqi oil via Kuwait and tapping Iraq as a partial solution to Kuwait's growing demand for natural gas. The committee also is looking at ways to encourage Kuwaiti investment in southern Iraq. However, security and political sensitivities remain a large concern for Kuwaiti companies. Al-Own said Kuwait is committed to engaging the new Iraqi government on these issues, but he stressed that American support for Iraq would be necessary for years to come if these and other energy issues are to be successfully resolved. End Summary.

(SBU) Bilateral Technical Committee Formed

12. (SBU) In a March 2 meeting with Econcouns, Econoff (notetaker) and visiting officials from the U.S. Defense Energy Support Center (DESC), Undersecretary for Oil Issa Al-Own said Kuwait and Iraq have recently created a technical committee to begin resolving bilateral energy concerns and to find areas for future mutual cooperation. "Kuwait is talking to the Iraqis directly and looking for the development of strategic cooperation between the two countries," Al-Own said. He reported that the technical committee, which "has the blessing of the Prime Minister," has met three times in Kuwait since December 2003 (December 11, January 17, February 29) and the next meeting is scheduled for May 4, 2004. The Undersecretary heads the Kuwaiti delegation, which is composed of chairmen from the production, marketing and refining sectors representing the oil, gas, and related commercial industries. Although Al-Own described the Iraqis as committed to the work of the committee, he told us Iraqi politics handicap Iraq's energy operations. He expressed concern that he would be dealing with "new faces" after the June 30 transfer of sovereignty to a transitional Iraqi government.

(U) Kuwait Supplying Fuels to Iraq: How Much for How Long?

13. (C) Al-Own said the Iraqis informed the technical committee that Iraq would need 6.2 million liters of fuels a day, beginning April 1st. He said he was uncertain how Iraq arrived at this figure, but stressed he hoped it had been decided in close coordination with the USG. Al-Own said Kuwait is prepared and able to supply 3.6 million liters/day to Iraq, but more than that would be logistically difficult to accomplish due to loading and transport limitations. He said he suspected Iraq's oil production and refining would be crippled for a long time, and thus more permanent solutions, such as new pipelines, would be needed to meet Iraq's growing fuel needs. Al-Own estimated that it would take Iraq seven to nine years to get back on its feet in terms of production. Referring to the Iraqi State Oil Marketing Organization (SOMO), he said he was "not confident of SOMO's capabilities to transport and pay" for any fuels received, and that the only way to ensure continuity would be to have the "Americans lay down the structure of operations, which Iraq must accept as reasonable."

14. (C) DESC officials briefed the Undersecretary on the state of commercial negotiations to find a replacement for the current KBR administered humanitarian needs contract due to expire March 31. Al-Own appeared satisfied with how these contracts were being negotiated. He emphasized the need for

all contracts to be openly bid, and for the winners to comply with all safety and trucking specifications. He said that this contract represented "a new situation, an open opportunity, and it is in the interests of all parties to comply."

(SBU) Future Export of Iraqi Oil via Kuwait

15. (SBU) Al-Own said Kuwait is considering Iraq's recent request to export a portion of Iraqi crude oil through Kuwait's ports. He explained that Iraq originally had asked that one million barrels per day be exported via Kuwait, but now reduced its request to 250,000 barrels/day. He said Kuwait was already intending to expand its export facility from the current capacity of two million barrels/day to a capacity of three million/day within seven years and to four million/day within 15 years. Any new expansion plans will factor in the additional Iraqi shipments, Al-Own said. He expected a technical team to have preliminary cost estimates for such a project within the next two months, although he emphasized there are major hurdles to this effort, particularly since there currently are no functioning oil pipelines that can be used to accommodate the Iraqi shipments.

(SBU) Kuwait's Growing Demand for Natural Gas

16. (SBU) Al-Own described the challenge of securing much-needed new supplies of natural gas for Kuwait as a "headache" for him as Undersecretary. (Note: Although Kuwait is blessed with extensive oil deposits, it has insufficient natural gas supplies. End note.) Al-Own explained that Kuwait needs additional natural gas for two purposes: power generation and the growing petrochemical industry. Kuwait wants to convert its oil burning energy plants to more efficient and clean natural gas. Likewise, Kuwait is expanding its petrochemical industry, with a \$6 billion deal with Dow Chemical being the cornerstone of this expansion.

17. (C) Al-Own said Kuwait is exploring four separate options, or a combination thereof, for securing this needed natural gas and said a final decision would be made sometime this year. One option is a project with Qatar that could potentially provide 1.2 billion cubic feet of gas per day. Al-Own said ExxonMobil is exploring this project and would be in Kuwait for renewed talks in May of this year. Kuwait was also considering imports of natural gas from Iran (Reftel A). Another possibility was to develop the offshore Al-Durra gas fields in connection with Saudi Arabia and Iran, but he said the dispute with Iran regarding their competing claims on the field would need to be resolved first.

18. (C) The final option under consideration by the technical committee is for Iraq to provide some natural gas to Kuwait. Al-Own said from 1986-1990, prior to the first Gulf War, Iraq provided Kuwait with 200-300 million cubic feet per day, but much of the gas was "wet" and therefore of inferior quality. Importing Iraqi gas would further enable consumers to rationalize their use of Kuwaiti gas for maximum efficiency. Under such an export plan, Iraq would no longer need to flare its gas, resulting in reduced pollution and increased export revenues. Al-Own said the infrastructure was in place for these deliveries to begin again, noting that a connected gas pipeline was in good condition, although metering instruments would need to be installed. He, however, remained concerned about the quality of the gas from Iraq. Econcouns asked about possibly entering into a gas for debts swap with Iraq, which Al-Own said was a possibility but that Kuwaitis still harbor a lot of animosity towards Iraq for the damage caused in 1990-91, for which they still demand compensation.

19. (C) Equate Petrochemical Company (a joint venture of Dow Chemical and Kuwait Petroleum Investment Company) has previously expressed to us strong interest in purchasing Iraqi gas for its Kuwait facility. Additional supplies of gas would allow Equate to fully utilize its plant's capacity and boost its profitability. Equate also expressed its willingness to make the necessary minor upgrades to the pipeline system in return for a supply contract.

(C) Kuwaiti Investment in Iraq: Wait and See

110. (C) Iraq, through the technical committee, has asked Kuwait to encourage investment in Iraq's energy sector in an effort to help revitalize that sector. When Econcouns asked about the possibility of the two countries jointly developing the Rumaila oil fields as a means of encouraging Kuwaiti investment, Al-Own said the committee considered this issue at its first meeting, but due to the political sensitivity of the subject, Iraq had asked that this issue be tabled. (Al-Own recalled that Saddam Hussein's regime's demand for control of these fields was one of Iraq's primary

reasons for launching the 1990 invasion.) Due to the sensitivity surrounding the idea of joint exploitation of the Rumaila fields, this part of the technical committee's discussion was not even recorded into the meeting's minutes, Al-Own said. Plans, however, are currently being considered to open a Kuwaiti investment office in Basra, but the security situation remains a concern. Such an office could help facilitate various outsourcing contracts with Kuwaiti firms, helping bring the energy sector back on line more rapidly.

(U) Comment

11. (C) Al-Own frankly discussed the efforts Kuwait and Iraq are currently undertaking to rebuild the energy sector and to mutually improve bilateral relations. He stressed, however, that any solutions would only be for the long term and that Iraq would continue to rely upon US assistance for the foreseeable future. He said Kuwait remains committed to helping the US achieve success in Iraq, recognizing the dire implications for Kuwait otherwise. Post views this working level bilateral energy committee as a positive step for Kuwait-Iraq economic and strategic partnership relations. We will continue to monitor its progress and undertakings. Baghdad minimize considered.

JONES